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DIRECTORATE OF
INTELLIGENCE

Intelligence Memorandum

The Economic Situation in South Vietnam

March 1973

USAID review completed

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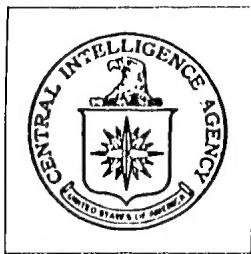
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March 1973

The Economic Situation in South Vietnam
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Although major supply shortages resulting from road interdiction have been alleviated, prices increased steadily during March and are now up 11% for the year to date. Further government import restrictions have been imposed to curtail drawdowns of foreign exchange holdings. Black market dollar prices dropped sharply in the latter part of the month as importers were forced to come up with more piasters to fulfill the new import financing requirements.

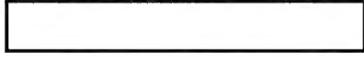
The Land-to-the-Tiller program marked its third anniversary on 26 March. It has achieved its goal of distributing one million hectares of land to former tenant farmers.

Although actual business investment was practically nil during 1972, development loan approvals increased notably as investors apparently continued to plan for future projects.

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DISCUSSION

Recent Developments*

1. South Vietnam's economic slump continues, with only limited signs of a pickup in activity appearing. The February supply shortages, resulting primarily from road interdiction -- particularly serious in the Central Highlands -- have been alleviated, and shipments of most commodities are now at nearly normal levels. There are, nevertheless, few signs of a recovery from the business recession, and spending by both consumers and investors remains at a generally depressed level. Two months after the cease-fire announcement, political and military uncertainty remains the major obstacle to a revival of business confidence.
2. Following a general decline in prices after the Tet holidays, price levels during March began climbing again, with the Saigon retail price index up by about 5.2% as of the 26th of the month. Since the beginning of the year, prices have increased by some 11%, with foodstuffs rising 10% and non-food items about 14%. The recent price increases reflect not only seasonal fluctuations in several perishable commodities, but also higher transportation costs resulting from the February increase in the official price of petroleum products. In addition, reports of renewed Viet Cong tax efforts along commercial routes and rumors that the government was soon to raise military and civil service cost of living allowances served to exert upward pressure on prices. More recently, upward movements in rice prices have been a major factor in the increase in the price index.

Rice Prices

3. Although rice shipments from the Delta have been slow for several months, rice prices remained stable throughout February and the first part of March. While government stocks of imported rice were adequate, stocks of domestic rice were declining. Therefore, on 6 March the Ministry of Economy acted to stimulate shipments from the Delta, especially to the northern rice-deficit provinces. Official wholesale prices of imported US rice, most of which is sold in the north, were increased 20%. The result has been that retail rice prices in Saigon increased about 8% during March. Because it is likely that the government will continue to adjust selling prices as a means of ensuring movement of domestic rice out of the Delta, further price increases can be expected.

* Charts showing major economic indicators and the government budget follow the text.

Further Import Restrictions

4. In view of increased import requirements for reconstruction and business recovery combined with uncertainty concerning future foreign exchange availabilities, the government in early March took further steps to ration its declining reserves and to limit commodity imports to those items considered most essential. Advance deposit requirements, raised initially in late February, were increased again in early March on imports financed by both the United States and South Vietnam. Additional advance deposit requirements were also placed on a number of luxury items including air conditioners, television sets, radios, and refrigerators and on some foodstuffs such as beverages. For US-financed imports, the retention period of deposits by the government was extended from three to six months. The most significant move, however, was an increase of the exchange rate for US-financed imports from 330 to 360 piasters per dollar. Although the net effect of these measures is not yet apparent, it is probable that the demand for imports, particularly luxury items, will be curtailed.

Currency Markets

5. Currency and gold black markets have fluctuated widely during the past several weeks, reflecting the world monetary situation, the dollar devaluation, and domestic speculative activity. The black market price for dollars jumped during the first week of March, reaching a peak of about 580 piasters per dollar, more than 100 piasters above the official exchange rate. By 26 March, however, the rate had fallen to 540 piasters per dollar. The price of gold leaf followed a similar pattern, reaching a peak of 45,600 piasters per troy ounce (about \$96) and dropping off to 37,700 (about \$79). The declines are at least partly attributable to a cash and credit squeeze in the private sector resulting from both the government measures on imports mentioned above and a decrease in bank loan/deposit ratios that has reduced funds available for loans. The black market for Military Payment Certificates (MPC) was abruptly halted on 15 March when this means of payment was discontinued. An increased supply of dollars resulting from the demise of MPC may also have been a factor in the fall of black market dollar prices.

Land Reform Program Meets Goal

6. The Land-to-the-Tiller program, which marked its third anniversary on 26 March, has achieved the original goal of distributing one million hectares (about 2.5 million acres) of land free to new owners. As of 26 March, titles had been issued to 650,000 farm families, for just over one million hectares of land. Although distribution of land titles has been moving along according to schedule, government compensation to former

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land owners has been slower. Despite efforts to increase the pace of compensation, payments made to date still cover only about 50% of the total land distributed.

7. The attainment of the government goal of land distribution does not signal the end of farmland allocation. Preliminary government agricultural development plans call for a large expansion of cultivated land which will be distributed to new settlers over the next five years. From a base of 2.5 million hectares now under cultivation, the goal is to reopen about 500,000 hectares of abandoned lands and to bring into production an additional 1.2 million hectares of previously uncultivated land. The mechanics for distribution of these new lands are as yet unclear. Although such a program will probably be fashioned after the Land-to-the-Tiller program, the current limits on plot size of 1-3 hectares per family probably will have to be increased because of the hilly terrain and type of soil found in Military Regions 2 and 3, where much of the new land is located. Some new land already has been opened up in connection with refugee resettlement, but a large-scale program, which could stimulate movement back to the countryside and significantly increase agricultural output, will have to await an improvement in security.

Development Loans

8. Although actual business investment was practically nil during 1972, investors apparently continued to plan for future projects. Recent reports on the activities of government-sponsored development financing institutions during the past year indicate a notable increase in loan approvals, particularly since the passage of the new liberalized investment law of June 1972. Once security conditions improve, this increase in loan commitments could provide the basis for substantial increases in the level of private sector investment.

9. One of the major funding mechanisms for these loans is the National Economic Development Fund (NEDF) established in March 1972 to provide medium-term and long-term credits to intermediate credit institutions for private investment projects. The NEDF, initially set up with 10 billion piasters (\$21 million) from US aid counterpart funds, is administered by the National Bank of Vietnam, but functions autonomously with its own board of directors. It is also authorized to accept grants or loans from foreign governments in any foreign currency and could be used as one of the primary means of channeling foreign aid to productive investments in South Vietnam. Intermediate financial institutions that receive a major share of their loanable funds from the NEDF include the government-owned Industrial Development and Agricultural Development

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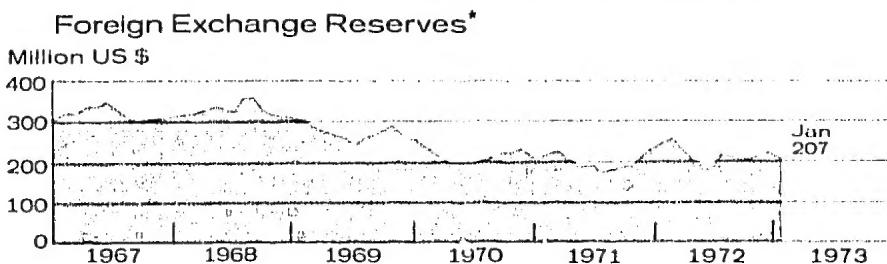
Banks (IDB and ADB) and the joint government/private bank-owned Financial Society for the Development of Industry in Vietnam (SOFIDIV).

10. Reports on activity of the IDB during 1972 indicate that 70 medium-term loans totaling some 5.5 billion piasters were approved, compared with loans of only 1.3 billion in 1971. Of the loans authorized in 1972, about 25% were allocated to industries processing foodstuffs and marine products; 20% for the textile industry; 19% to the metal, equipment, and electronic industries; and the remainder to water, electric power, and transportation projects. Credit approved by SOFIDIV in 1972 totaled about 3.2 billion piasters for some 27 investment projects in a variety of industrial undertakings. In the agricultural sector, the ADB increased loans from a total of 10 billion piasters in 1971 to 18.9 billion in 1972.

11. With the exception of ADB funds, only a small proportion of the approved credit was actually disbursed last year. Furthermore, there is little evidence to suggest that any of the projects approved by the intermediate institutions have got off the ground during the year. For example, funds committed by the NEDF to intermediate institutions in 1972 were estimated to be around 8 billion piasters, while actual disbursements were only about 1.3 billion piasters. Even if disbursements during 1973 increased significantly, the Mission in Saigon estimates that most projects would not be completed until some time in 1975.

Figure 1

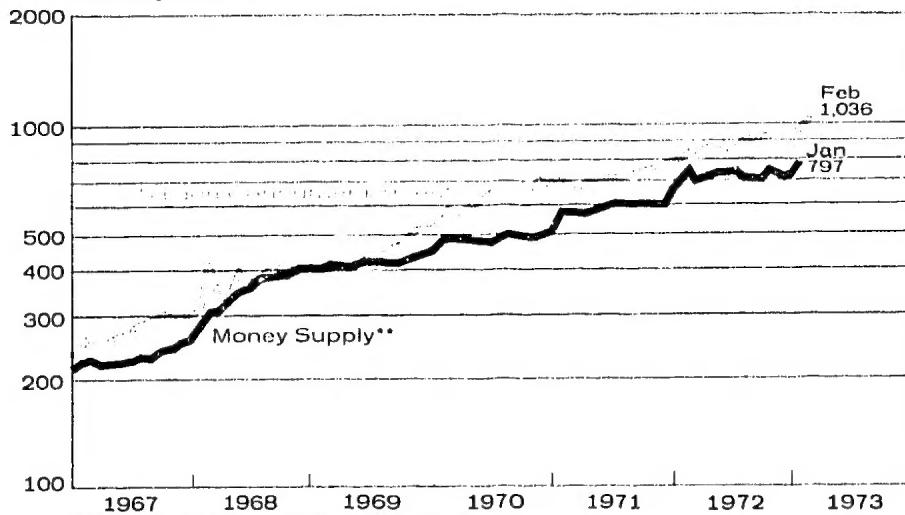
South Vietnam: Economic Indicators



*Consisting of gold and foreign exchange held by the National Bank of Vietnam.

Indexes of Money Supply and Saigon Consumer Prices

January 1965 = 100

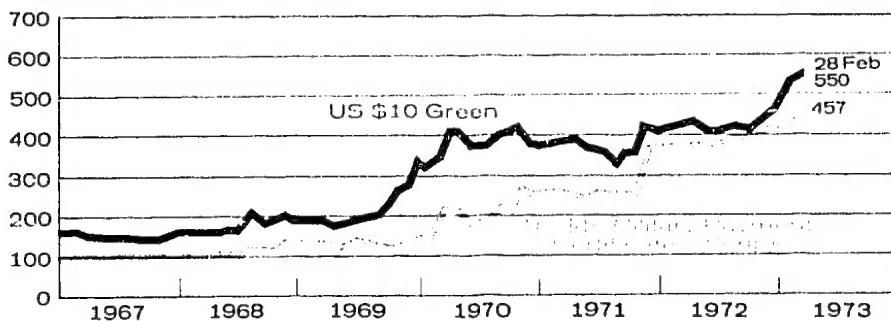


*USAID monthly average retail price index for Saigon.

**Data are for end of month.

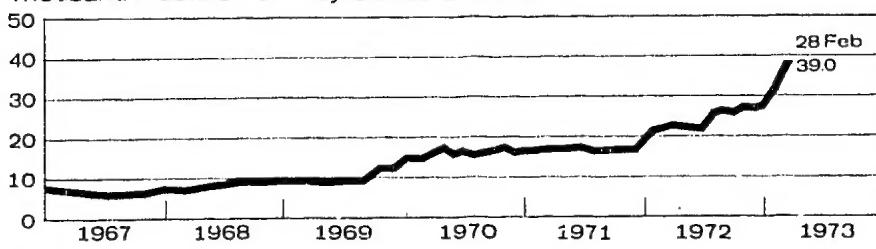
Free Market Currency Prices

Piasters Per US \$



Free Market Gold Prices

Thousand Piasters Per Troy Ounce Gold Leaf



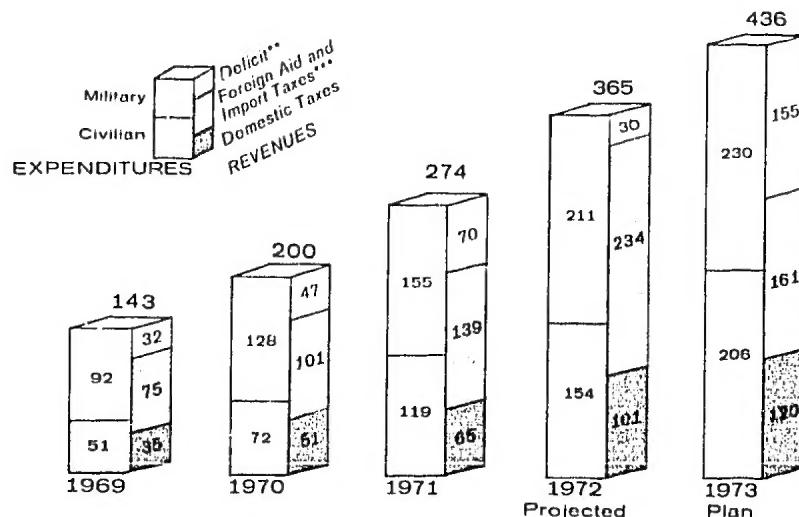
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Figure 2

South Vietnam: Government Budget*

Billion Piasters



*Data include extrabudgetary revenues and expenditures.

**Residual. Financed primarily by borrowing from the National Bank.

***Includes customs duties and other import taxes, counterpart funds generated by US-financed import programs, and profits from foreign exchange transactions.

A major result of the November 1971 reforms was to make explicit a greater share of US aid to the budget that earlier took the form of high customs duties on aid-financed imports.

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